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IN THE

Supreme Court of the United States

OCTOBER TERM, 1959

No. 996 136

CONSOLIDATED TITLE CORPORATION, a Maryland corporation, *Petitioner*

v.

DISTRICT OF COLUMBIA, *Respondent*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

JOHN J. WILSON
PHILIP S. PEYSER
815 15th Street, N. W.
Washington 5, D. C.

THOMAS S. JACKSON
719 15th Street, N. W.
Washington 5, D. C.

Attorneys for Petitioner

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DISTRICT OF COLUMBIA, *Respondent*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Consolidated Title Corporation, a Maryland corporation, Petitioner herein, prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in Nos. 15,120 to 15,138, inclusive, entered February 25, 1960, and on a Petition for Rehearing, the Order denying the same entered April 1, 1960.

CITATIONS TO OPINIONS BELOW

The opinion of the District of Columbia Tax Court is reported at 87 W.L.R. 288; D.C. C.T. 1653, and is printed at page 36 of the Joint Appendix. The opinion of the United States Court of Appeals for the District

of Columbia Circuit is reported at U. S. App. D.C. , 275 F. 2d 885, and is printed at page 5a of the Appendix to this Petition. The order of the United States Circuit Court of Appeals denying the petition for rehearing is reported at U. S. App. D.C. , 275 F. 2d 885, and is printed at page 8a of the Appendix to this Petition.

JURISDICTION

The judgment of the United States Court of Appeals for the District of Columbia Circuit was entered February 25, 1960. Rehearing was denied April 1, 1960 (Appendix, pp. 7a, 8a). The jurisdiction of this Court is invoked under the provisions of 28 U.S.C. Section 1254(1).

QUESTION PRESENTED

This case presents the question of the taxability under the District of Columbia Revenue Act of 1939 and the Income and Franchise Tax Act of 1947, as income from District sources, of dividend distributions to Petitioner, a non-resident corporation, found by both Courts below to be not doing business in the District of Columbia. Subsidiary questions grow out of the fact that the Courts below failed to pass upon the effect of a provision of the District of Columbia statute exempting the subsidiary, operating title insurance corporations from the payment of income tax and the ruling that no apportionment was required, although the source of the earnings of the subsidiary, operating title insurance corporations was in substantial part from their operations in Maryland and Virginia. The case presents the further constitutional question under the Fifth Amendment as to whether Petitioner is not deprived of its property without due

process of law in requiring it to pay accumulated taxes, penalties and interest for nineteen years in the course of overruling the only judicial decision as to the scope and meaning of *income from District sources.*

STATUTES INVOLVED

District of Columbia Revenue Act of 1939, approved July 26, 1939, Public Law No. 225, 76th Congress, First Session, Chap. 367 and District of Columbia Income and Franchise Tax Act of 1947, Public Law No. 195, 80th Congress, First Session, Chap. 258 (cited provisions are printed in Appendix hereto).

STATEMENT OF THE CASE

Petitioner was organized in 1934, under the laws of the State of Maryland as an instrumentality in carrying out a plan of reorganization of Washington Consolidated Title Company in and approved by the Bankruptcy Court in Baltimore, Maryland. The bankrupt corporation owned more than 75 percent of the capital stock of each of three title insurance companies which operated in the District of Columbia, Maryland and Virginia. Under the provisions of its corporate charter, Petitioner was under the control of a Committee of Creditors who were given all of the controlling Class A stock. The Committee managed Petitioner until its bonds were paid off in 1945.

Respondent has asserted against Petitioner taxes for the years 1939 through 1957 under the Revenue Act of 1939 and the Income and Franchise Tax Act of 1947. The sole source of Petitioner's income was dividends received from the three operating title insurance companies which did business in Virginia and Maryland, as well as the District of Columbia. The Tax Court found that Petitioner was not engaged in commercial

activity or in any trade or business in the District of Columbia (JA 49), and the Court below did not change that finding.

Notwithstanding its holding that Petitioner was a non-resident corporation and was not doing business in the District of Columbia, the Tax Court held that the dividends paid by the three operating title insurance companies during all the years involved constituted taxable income to the Petitioner in each of said years. The basis of the Tax Court decision, which was affirmed by the Court below, was that these dividends were taxable as income from District of Columbia sources.

In connection with the business of the three operating title insurance companies, Petitioner offered to prove that they search title, issue title certificates and insurance policies in the District of Columbia, in several counties in Maryland, and in several counties and cities in Virginia; that as a result, these three companies have had income from sources outside of the District of Columbia; that the income from such sources is substantial; and that such sources of income go into the general funds of the three title insurance companies and "as far as Consolidated is concerned, come out in the form of a dividend" or become "a base for the payment of a dividend" to Petitioner. The Court sustained objections to this line of testimony and appropriate tenders were made (JA 79, 80). The Tax Court held that this income was not subject to apportionment because the Commissioners had adopted no formula for apportionment in these circumstances and therefore all of said dividend income must be "*allocated* in its entirety to the District of Columbia." (JA 52).

The three operating title insurance companies paid to the District of Columbia a tax equal to two (2%) percent of their net premium receipts under the provisions of Title 47, Section 1806 of the D. C. Code (1951) (JA 81, 82). By the terms of this statute,[1] this tax is "in lieu of all other taxes" and these companies are not required to pay income and franchise taxes to the District of Columbia. For the nineteen-year period 1939 to 1957, taxes paid by these operating title insurance companies to the District of Columbia aggregated $129,664.49, or a yearly average of over $6,800 (JA 83). Petitioner contends that the exemption granted these operating title insurance companies by reason of payment of the net premium receipt tax prevented the District of Columbia from taxing their distributions to Petitioner as dividends subject to income or income and franchise tax.

The total amount of taxes, penalties and interest assessed against and paid by Petitioner for the nineteen years was $206,112.56 (JA 62). The taxes are imposed not only for the more recent years but also for the six years in which Petitioner was under the control of the Committee of Creditors growing out of the bankruptcy proceeding in Baltimore.

[1] The Court of Appeals held in *Real Estate Title Insurance Company v. District of Columbia*, 82 U.S. App. D.C. 170, 161 F. 2d 887, that Section 1806 and not Section 1702 applies to title insurance companies.

REASONS FOR GRANTING THIS WRIT

The decision below is not in accord with applicable decisions of this Court as to the taxation of non-resident corporations, not engaged in business in the jurisdiction, and as to the lack of power to tax earnings attributable to other jurisdictions without apportionment. The case also presents an important question not hitherto decided by this Court, as to the constitutional limitation of judicial power in overruling the settled construction of a tax statute, with resulting imposition of taxes, penalties and interest for nineteen years.

The primary question in this case relates to the statutory construction of the following provision of the Income and Franchise Tax Act of 1947 relating to taxation of corporations:

TITLE X.

"§ 47-1580. *Purpose of article.*

> "It is the purpose of this article to impose (1) an income tax upon the entire net income of every resident and every resident estate and trust, and (2) a franchise tax upon every corporation and unincorporated business for the privilege of carrying on or engaging in any trade or business within the District and of receiving such other income as is derived from sources within the District:"

In numerous cases the District of Columbia Courts have construed this Act as imposing an income tax on individuals and a franchise tax on corporations, e.g. *District of Columbia* v. *Southern Railway Company*, ___ U.S. App. D.C. ___, ___ F. 2d ___, decided on the same day, February 25, 1960; *Smoot Sand & Gravel Corp.* v. *District of Columbia*, 104 U.S. App. D.C. 292, 261 F. 2d 758; *District of Columbia* v. *Radio Corporation of America*, 98 U. S. App. D.C. 119, 120, 232 F. 2d 376. Petitioner contended that it was a non-resident corporation, not engaged in business in the

District of Columbia, and therefore it was not subject to the tax. The Tax Court found as a fact that Petitioner was not engaged in business or in commercial activity in the District of Columbia and the Court of Appeals did not disturb that finding. Both Courts held that Petitioner was subject to tax because the dividends constituted income from District sources and were therefore taxable, even though Petitioner was not doing business therein. In so holding, the Courts below have ruled contrary to numerous decisions of this Court that the doing of business or engaging in commercial activity is the legal basis and prerequisite for a franchise tax. *Zonne* v. *Minneapolis Syndicate*, 220 U. S. 187, 55 L. ed. 458; *McCoach* v. *Minehill*, 228 U. S. 295, 57 L. ed. 842, 847; *United States* v. *Emily Bird Thayer Real Estate Company*, 227 U.S. 28, 59 L. ed. 825.

The same statute imposes an unincorporated business tax upon individuals engaged in business activity which is capable of being performed as a corporation. This tax is imposed upon both residents and non-residents. Based primarily upon the analogy of the tax to that imposed upon corporations, the Court of Appeals held in *District of Columbia* v. *Pickford*, 86 U.S. App. D.C. 17, 179 F. 2d 271, that only the income attributable to business activity was subject to the tax. In its decision therein the Court cited and relied upon the above-mentioned decisions of this Court.

The effect of this construction is to give this general language of the statute the broadest application which would include within its ambit all income that the Congress could constitutionally tax for the benefit of the District of Columbia. Under this construction, the denomination of the tax as a *franchise tax* is mislead-

ing and confusing because by definition and use, a franchise tax is one that is imposed upon the privilege of doing business; here the tax is imposed even though it was found as a fact that Petitioner was not doing business or engaged in commercial activity in the District of Columbia. Furthermore, the entire first clause becomes meaningless because in this case Petitioner has not enjoyed the privilege of doing business in the District of Columbia but is nevertheless held to be subject to the tax. In the only comparable State decision that has been found, the Court of Appeals of Kentucky held that the principle of *ejusdem generis* required that the word "*sources*" be construed narrowly, in relation to the business done in that State, and that the statutory imposition of the tax upon income from sources in Kentucky, did not make taxable dividends paid by corporations operating in Kentucky to their non-resident parent corporation. *Atlantic Coast Line R. Co. v. Commonwealth*, 302 Ky. 36, 193 S.W. 2d 749, 758. Compare also *Williams v. American Refrigerator Transit Co.*, 91 Ga. App. 522, S.E. 2d 336.

This Court has held that the constitutional incidence of a tax on dividends is the earnings and profits of the distributing corporation. *Brainard v. Hubbard*, 12 Wall. 1, 10; 20 L. ed. 272, 275. In *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435, 446, 85 L. ed. 267, 271, this Court held that a tax on non-residents on account of Wisconsin's allocated portion of earnings distributed as dividends, could be sustained as an additional income tax applicable at the time of distribution. See also *International Harvester Co. v. Wisconsin*, 322 U. S. 435, 443, 88 L. ed. 1373, 1380.

In the present case both Courts below refused to consider the fact that the sources of a substantial

portion of these dividends were the business activities of the operating title insurance companies in the States of Maryland and Virginia. Since the essential nature of a tax on dividends is a deferred tax upon the income of the distributing corporation, this income necessarily was partly from sources outside of the District of Columbia and therefore not subject to tax. The statute under consideration provides for apportionment where the income is in part from sources outside the District (D. C. Code 47-1580a). In *Panitz* v. *District of Columbia*, 74 App. D. C. 284, 122 F. 2d 61, it was held that the constitutionality of a District of Columbia franchise tax on a non-resident corporation could be sustained only when the tax was reasonably related to the income attributable to the District of Columbia. Compare *District of Columbia* v. *Evening Star Newspaper Co.*, 106 U. S. App. D.C. 360, 273 F. 2d 95, decided December 10, 1959.

The decision in this case is not in accord with the decision of this Court in *Hans Rees' Sons* v. *N. Carolina ex rel Maxwell* (1931), 283 U. S. 123, 138, 75 L. ed. 879, 905. There, this Court was asked to determine the validity of an apportionment provision applied by the State of North Carolina with respect to a corporate taxpayer doing business in another state. Evidence was offered to show that the apportionment formula was arbitrary and unconstitutional, because no allocation was made with respect to out-of-state earnings. The Supreme Court of North Carolina had held that the taxpayer constituted a unitary business and for this reason no apportionment need be made. This Court reversed that decision, holding that the refusal to consider the tendered evidence as to the out-of-state earnings constituted prejudicial error and a denial of the taxpayer's constitutional right to due process.

The facts in the present case amount to a complete parallel of those considered in the above-cited decision of this Court.

Dividend distributions of corporations operating in the District of Columbia are not usually taxable when received by another corporation because the statute exempts from taxation distributions made by a corporation which is subject to said Act. The purported exception in this instance arises from the fact that the title insurance corporations pay a tax under the provisions of Title 47-1806 of the District of Columbia Code, instead of a strict income tax. However, this statute provides that the tax paid by these title insurance companies "shall be in lieu of all other taxes". The Courts below refused to give any weight or consideration to this provision. It is submitted that since under the doctrine of *Wisconsin* v. *Penney*, *supra*, a tax on dividends is a deferred tax on the income of the corporation, this statutory exemption from other taxes should have the effect of preventing the distributions of said corporations out of their earnings and profits from being taxed as dividends. Moreover, such an interpretation would be in harmony with the general provisions of the statute which are to tax the earnings of corporations only once and not to tax dividends distributed to other corporations.

The term *income from District sources* was used in both the 1939 and the 1947 Acts. The only known judicial construction of the term was made by the Board of Tax Appeals of the District of Columbia in *Community Finance Corporation* v. *District of Columbia*, 72 W.L.R. 737, decided July 13, 1944. The Board of Tax Appeals gave thorough consideration to the problem and drew a parallel with the provisions

of the 1939 Internal Revenue Code, which had been enacted only shortly before the District law. While the provisions of the Code were specific as to what constituted income from sources within the United States, the language of the District of Columbia statute was only general in nature. Specifically the Board held that payments of interest by residents of the District to a Virginia corporation, not doing business in the District, did not constitute income from District sources that was taxable to the corporation. The case was presented as a test case but was not appealed. The decision of the Board was in line with the District of Columbia statutes and decisions which do not tax non-residents or residents domiciled elsewhere.

The present decision denotes a change of tremendous importance. It is based upon the broadest possible construction of the statute. It is fundamentally contrary to the concept of a franchise tax. The principle underlying the decision would be equally applicable to dividends paid by banks and public utilities, which pay a gross receipts tax in lieu of an income tax. The stock of such corporations as Potomac Electric Power Company is widely held, and the effect of this decision would require a non-resident corporation not only to pay a tax in the District of Columbia on the dividends received, but also under the provisions of Title 47-1546 to take out a license to receive such income from District sources. It is submitted that this construction of the statute is fundamentally unsound and inconsistent with its other provisions, and results in the taking of Petitioner's property without due process of law, in violation of the Fifth Amendment of the Constitution. If such a statute and construction should be adopted by other states, it would have the

effect of preventing investment in the securities of District of Columbia public utilities and banks by non-resident corporations.

With respect to Petitioner, this drastic change in judicial construction results in the imposition of taxes, interest and penalties accumulated over nineteen years. Such accumulated taxes, imposed all at one time, constitute an unconscionable and unbearable burden. Certainly the constitutional requirements of due process place some reasonable limitation and restriction upon retroactive judicial construction, in the same way that the constitutional limitations apply to retroactive legislation. *Welch* v. *Henry*, 305 U. S. 134, 150, 83 L. ed. 87, 95.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that this Petition should be granted.

Respectfully submitted.

JOHN J. WILSON
PHILIP S. PEYSER
815 15th Street, N. W.
Washington 5, D. C.

THOMAS S. JACKSON
719 15th Street, N. W.
Washington 5, D. C.

Attorneys for Petitioner

June 10, 1960